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Before the
FEDERAL COMMUNICATIONS COMMISSION
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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of)

Implementation of Sections of)
the Cable Television Consumer)
Protection and Competition Act)
of 1992)

Rate Regulation)

MM Docket No. 92-266

JOINT COMMENTS OF BEND CABLE COMMUNICATIONS, INC., CABLE
MANAGEMENT CORPORATION AND RIVER VALLEY CABLE TV

Bend Cable Communications, Inc., Etan Industries, Inc.
and River Valley Cable TV (the "Companies"), by their
attorneys, hereby submit their comments in response to the
Commission's Further Notice of Proposed Rulemaking ("Further
Notice") in the above-captioned proceeding.¹

The Companies are participating in this Further Notice
because the regulations that the Commission adopted in its
"benchmark/price cap" order do not adequately address the
needs and problems of small cable companies. These comments
will offer several constructive suggestions for easing the
administrative burdens and harsh regulatory impact of rate
regulation on small companies. The Companies are not asking
for an outright exemption, but only a less burdensome means
of attaining a fair return on investment.

By now, the plight of small cable companies and systems
serving low density areas has been brought before the

¹ See Memorandum Opinion and Order and Further Notice
of Proposed Rulemaking, MM Docket No. 92-266, FCC 93-389
(released August 10, 1993).

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Commission by various coalitions of small operators as well as by members of Congress.² The Companies support these submissions, emphatically pointing out that the prospect of doing business under either the current benchmark/price cap approach or under the form of cost-of-service regulation that traditionally has existed in the utility field are equally daunting.

The Companies are encouraged by the degree of Commission concern for the plight of small systems evidenced by the Further Notice; however, the continuing focus only on systems serving under 1,000 subscribers remains troubling. The Companies are concerned that in focusing only on systems serving under 1,000 subscribers, the Commission is neglecting the pressing and legitimate needs of the stand-alone operator and the small company serving low density rural areas. The Companies strongly urge the Commission to expand its analysis beyond the 1,000 subscriber limit to include the impact of the new rate regulations on single system operators, small MSOs and systems serving low density areas. As explained

² See e.g., Petitions for Reconsideration of the First Report and Order in MM Docket 92-266, filed by Coalition of Small System Operators, Community Antenna Television Association, Inc.; Comments of Prime Cable, et al. and Comments of Small Business Administration in MM Docket 93-215 (Cost-of-Service Rulemaking) filed August 25, 1993; Letter from Senator Lauch Faircloth to Commissioner Quello (July 22, 1993); Letter from Senator John Breaux to Commissioner Quello (August 3, 1993); Letter from Senators Bob Packwood, Bob Dole, Conrad Burns, Ted Stevens, Larry Pressler and John McCain to Commissioner Quello (July 21, 1993).

below, this can be accomplished quite simply within the existing benchmark regulations without compromising the integrity of the Act.

I. Background

Bend Cable Communications, Inc. and River Valley Cable TV both are single-system operators.³ Etan Industries, Inc. technically is an "MSO," in that Etan and affiliated companies operate multiple systems; however, its 40 headends serve only 44,461 total subscribers -- an average of just slightly over 1,000 subscribers per headend.⁴ Although each Company operates one or more systems serving more than 1,000 subscribers, none of the Companies has the administrative and economic resources of large MSOs -- namely, large corporate administrative staffs; centralized data processing, billing, management, engineering and construction support; or substantial volume discounts on programming and equipment; readily available to larger MSOs.

³ Bend Cable Communications, Inc. operates a single system serving 16,000 subscribers in the Central Oregon community of Bend and one neighboring jurisdiction. River Valley Cable TV serves approximately 3600 subscribers in eleven rural townships and communities in the Central Pennsylvania counties of Clinton and Centre.

⁴ Etan Industries and affiliated companies operate systems are located in Louisiana, Mississippi, Texas and Nevada

Compounding the problem, the Companies -- like most small operators -- also serve areas of lower than average population density. Because of the differences in customer density per mile, the average capital investment per customer typically is significantly greater for a rural, small cable system as compared to its suburban counterpart. The system operating expenses in lower density areas also are higher and volume discounts are not available.

Even though they are small companies operating outside major metropolitan areas, each of the Companies believes that its subscribers deserve the best service possible at an affordable price. Each Company has a high level of commitment to the communities it serves, as demonstrated by local programming and community service. Bend Cable, for example, covers local high school sports, meetings of local governmental bodies and community events such as local charity auctions. In addition, Bend recently joined other local businesses in co-sponsoring the Cascade Cycle Classic, an event on the professional cycling tour and produced highlight shows that aired nightly on cable. Bend also participates in "Pay to Play," a community program that provides high school students an opportunity to earn money needed to participate in athletics, which can no longer be funded out of the local school budget. The Commission always has recognized the value of diversity of ownership and local

ownership of the media; unfortunately, unless small companies receive some meaningful relief, only large operators will be viable and concentration of the media will greatly increase.

II. Benchmark Modification for Stand-Alone Systems and Small Companies Serving Low Density Areas

Much of stand-alone and small operators' plight is linked to higher costs. Thus, the rate regulation approach that seems best suited to small systems and companies is cost-based. Yet, for a company with limited administrative resources, going through a classic cost-of-service proceeding would be prohibitive. On the other hand, while a benchmark process theoretically is less burdensome, the Commission's current rate benchmarks do not take higher small system costs into account.

The Companies therefore support an adjustment to the benchmark which would allow eligible systems to exceed by 10% the otherwise applicable benchmark rate for: (1) systems owned by independent operators with fewer than 50,000 subscribers; and (ii) systems that can document that they serve areas with fewer than 35 homes per mile. Such an approach would acknowledge the differences even though in most cases it would not fully compensate for the extra costs incurred by small operators.

III. Treatment of Taxes for Small Companies

Like many small businesses, the Companies have either a single owner or a limited number of shareholders, and, accordingly, have selected the Subchapter S corporation form of ownership to avoid double taxation of, in effect the same person. Pursuant to the Commission's Further Notice, the tax liability of a typical corporation would be included in its revenue requirement, even in years when the corporation pays no actual taxes.⁵ The Commission does not propose to allow taxes on earnings of S corporations to be included in the rate base, despite the fact that the shareholders of the S corporation are liable for taxes comparable to those incurred by other corporations. The effect of the FCC's proposal is to penalize small cable operators by reducing their revenue, simply because they have elected a form of business organization that is both customary and important to achieving other legitimate business objectives.

The courts consistently have considered and upheld taxes as includable expenses for Subchapter S corporations in rate-regulated industries. Although this issue apparently has not come up in a communications context (because telephone companies rarely are organized as S corporations), the issue

⁵ See Notice of Proposed Rulemaking, MM Docket No. 93-215, FCC 93-353 (released July 16, 1993) at ¶ 30 n.31.

has been addressed for other utilities. In fact, it is well settled that all tax liability associated with a public utility is properly included among cost of service expenses. In Galveston Electric Co. v. City of Galveston, the Supreme Court, in calculating the proper return on a utility's property, stated that "it is necessary to deduct from gross revenue the expenses and charges; and all taxes which would be paid if a fair return were earned are appropriate deductions. There is no difference in this respect between state and federal taxes or between income and other taxes."⁶

Indeed, the courts that have reviewed this issue have made clear that the income tax liability incurred by shareholders of S corporations is an unavoidable business expenditure that must be recognized as a cost of service. In Suburban Util. Corp. v. Pub. Util. Comm. of Texas, the Supreme Court of Texas held that although the utility itself did not pay federal income taxes, it was entitled to a cost of service allowance for federal income taxes.⁷ In reaching this decision, the court reasoned that

[t]he income taxes required to be paid by shareholders of a Subchapter S corporation on a utility's income are inescapable business outlays and are directly comparable with similar corporate taxes which would have been

⁶ 258 U.S. 388, 399 (1922) (emphasis added).

⁷ 652 S.W.2d 358, 364 (1983). Accord Application of B & B Water Systems, Inc., Docket No. 2351, 4 P.U.C. Bulletin 1528, 1531 (May, 1979); Application of Ingram Water Supply, Docket No. 2818 6 P.U.C. Bulletin 579, 586 (May, 1981).

imposed if the utility operations had been carried on by a corporation. Their elimination from cost of service is no less capricious than the excising of salaries paid to a utility's employees would be.⁸

In Moyston v. New Mexico Pub. Serv. Comm., supra, the court allowed the sole proprietorship to deduct taxes as expense, reasoning that "rates which fail entirely to take [federal and state income taxes] into account as operating expenses are unfair, unjust, unreasonable and discriminatory."⁹

The Commission has not articulated a reasonable basis for departing from well established rate regulation precedent on this issue. The Companies urge the Commission to rethink its position and allow S corporations to include all income taxes attributable to their operations in the rate base. By allowing these taxes to be included in S corporations' revenue requirements, the Commission will ensure that all forms of legitimate business organizations will be able to recover their actual costs and earn a fair rate of return.

IV. Conclusion

Although the Act directs the Commission to reduce the administrative burden of rate regulation on systems serving fewer than 1,000 subscribers, there are stand-alone systems

⁸ 652 S.W.2d at 364.

⁹ Id.

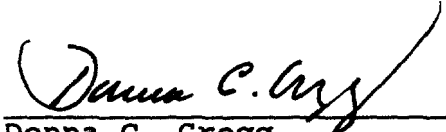
serving more than 1,000, small MSOs and companies serving areas of low population density on whom the burden of the new regulations falls with great harshness. To date, the only avenue for these systems to earn a fair rate of return is through a cost-of-service showing. That, in itself, will create additional burdens on small operators, the Commission and municipal franchising authorities. The simple benchmark modification recommended herein will improve the lot of the Companies and similarly-situated small and independent cable operators. The Companies also urge the Commission to rethink


and modify its current position on taxes of Subchapter S corporations.

Respectfully submitted,

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